

## Module XI: Understanding Insurance

**Summary:** *Everyone needs to have insurance, but most of us don't want to spend a lot of time dealing with it. This lesson provides just the basics: what you really need, what you may already have, and a discussion on a few other important topics. The first topic talks about why you need insurance and how it works. The second topic covers insurance that MOST of us need: Vehicle, Life, Property, and Health. Most adults need some kind of insurance because insurance helps prevent financial disasters.*

### So why does ANYONE need insurance?

The simple answer is “to avoid financial disaster.” In our society, we face the possibility of accidents, natural disasters, and illnesses that could devastate our lives financially. Just one unexpected event could cause a person to lose everything he or she had saved and acquired in a lifetime. Insurance allows you to reduce some of that risk by paying into a pool of funds with other people, all of whom hope a disaster never hits. When something does happen, the person can file a claim and get reimbursed. We typically have insurance to cover the risks of very large losses, which can occur because of accidents, illness, deaths, and liability lawsuits. To some degree, we insure ourselves based on how much risk we want to take with our finances.

All insurance policies have limits, which are the maximum dollar amounts that will be paid under the policy. You may hear insurance representatives talk about “indemnity.” This is the idea that insurance will cover only the actual amount of a loss, and not some inflated, false value. In other words, you can't insure an item worth \$500 for \$5,000,000 and, when it's stolen, file a claim and become rich. That would be gambling, and insurance companies don't do that. Some rules of thumb for deciding when you should get insurance are:

- Never risk a lot for a little. In other words, don't let a catastrophic loss go uninsured just to save a few dollars of premium.
- Never risk more than you can afford to lose.

Are you willing to risk having to pay living expenses if you are injured and can't work? Are you willing to replace expensive items if they are

lost or stolen? Are you willing to pay the costs of accidents and emergencies? Are you willing to leave your family financially unprepared in the event of your death?

If not, then you should consider your insurance options.

### **What is the purpose of insurance?**

1. **Sharing Risk:** As we discussed earlier, by pooling your money with others, all of whom hope disaster never happens, you share your risks with them. This allows the insurance companies to pay any claim you may have more easily because of the large amount of funds that they control and to which they have access.

2. **Protecting Against Liability:** “Liability” occurs when you are held responsible for the losses of others. Liability insurance pays for “the other person’s” losses. In most U.S. states, you must have at least liability insurance coverage to be legally allowed to drive a vehicle. Also, all U.S. military bases require proof of current liability coverage for you to get a permit to take a vehicle onto the base. We will discuss vehicle insurance more completely later in this lesson.

3. **Replacing Possessions:** Insurance can help you to replace your belongings after disasters such as fire, flood, and tornado, or if your vehicle is damaged, or if something is stolen. Without insurance on your possessions you could be left “starting over,” without furniture, clothes, or other daily necessities.

4. **Caring for Survivors:** Insurance such as life, health, and disability help take care of family members after an illness, accident, or death. When someone is sick or hurt, insurance helps cover medical expenses and loss of income. Life insurance can help survivors who were dependent on the insured person’s income to pay expenses and get their lives back together.

Let’s review the reasons you may need insurance:

- To prevent financial disaster caused by illness, accident, or a liability lawsuit
- To comply with vehicle insurance regulations

- To replace home, vehicle, or possessions that are lost or damaged
- To care for survivors in case of accident, illness, or death of wage earner

Remember to review your insurance needs regularly. As your life changes, your need for insurance changes!

### How does insurance work?

The basic payment you must make to have an insurance policy is called the **premium**. These payments are generally the same amount and must be paid regularly, such as monthly, quarterly, or annually. What you'll pay in premiums depends on the "group" you fit into according to the insurance company's and the industry's historical data. They compare you to their payout records to people similar to you, decide your risk category, and then set an appropriate premium. It is common for insurance companies to use an applicant's credit history as a factor in determining his/her insurance rating (Another reason to keep that credit record spotless!).

A **claim** is your request to the insurance company for reimbursement after an accident, illness, or loss. Insurance companies typically require you to fill out their claim form. Often, you must provide other documentation as well, like a police report and damage repair estimates. With health claims, doctors' offices often do the insurance paperwork for you.

Most insurance policies require you to pay a **deductible** any time you file a claim for insurance reimbursement. This is an initial set amount of money that you'll pay every time you file a claim for reimbursement, no matter how large the claim. It is one way that you "share" in the cost of insurance. For example, automobile collision deductibles typically range from \$100 to \$1,000. If you select a higher deductible, you will lower your premiums. Some insurance policies, such as health insurance, require that you pay part of the cost of a claim in addition to the deductible. This percentage is called "coinsurance." The amount you pay is called the **co-payment** or **co-pay**.

“Coinsurance” is a way for the insurance companies to share costs with customers and to reduce premiums. With “civilian” health insurance, it is common for you to pay 20% of your medical costs, and they’ll pay 80%, up to a certain maximum. The difference between a deductible and a coinsurance payment is that the deductible is a set amount; coinsurance is a percentage of the total bill.

### **Steps for filing a claim**

1. Contact your insurance company (IC)
2. Fill out claim forms
3. Keep IC informed of everything relevant to the loss
4. Gather all documentation to prove loss
5. Maintain contact with IC until claim is settled

If you disagree with the settlement offer, talk it over with your insurance agent. If you are still not satisfied, contact your state’s Insurance Commissioner. All states have a position similar to this that can provide a “third party” opinion to ensure that your treatment is fair. You may need to ask for the State Attorney General’s Office or Consumer Affairs Office for your state. Visit <http://www.inetbureau.com/ag.htm> for links to each state's Attorney General Office. This assistance is free, and an important consumer right. Take advantage of it.

### **What types of insurance do I need?**

When determining what insurance you need, keep in mind that insurance is designed to prevent financial disaster in case of illness, accidents, death, or liability lawsuit. You probably do NOT need special insurance for credit, air travel, renting a car, dreaded diseases, or your pets.

#### **A. Vehicle Insurance**

Most of us have (or at least drive) a car, truck, or motorcycle, and need insurance to do so. Do you know what insurance you have? Do you have all that you really need? This part of the lesson should

help you answer these questions. What does vehicle insurance cover?

- Liability for other drivers/vehicles
- Medical insurance
- Uninsured motorist coverage
- Physical damage to vehicle from many sources

“Automobile” insurance combines liability and property coverage on your vehicle(s) into a single-package policy. It can be purchased as full or partial coverage, for one individual or for a family. Your insurance agent will recommend minimum dollar amounts for each coverage type.

- Liability - Most states and ALL military installations require you to have liability coverage in order to drive there. “Liability” means your responsibility for other people’s losses. “Bodily injury” liability occurs when you (as car driver or owner) are held legally responsible for bodily injury suffered by other persons, including pedestrians. The coverage, or what the insurance company will pay out, is limited to a certain amount per person and a total per accident. “Property damage” liability occurs when you (driver or car owner) are held legally responsible for damage to other people’s property in an auto accident. This generally is their vehicle. This coverage is limited to a certain dollar amount, such as \$50,000. When deciding what coverage to have in your policy, remember that the typical bodily injury liability claim is more than five times the average property damage liability claim.
- Uninsured motorist - Many states also require you to carry insurance to cover your injuries and losses if you are in an accident with an uninsured motorist (and it’s his/her fault). This coverage is usually limited to set amounts per person, per accident, and for all property. It will be stated something like 25/50/20, meaning \$25,000 maximum per person injured, \$50,000 maximum per accident for everyone injured, and \$20,000 maximum for property damages.

- Physical Damage - Most people have insurance coverage for their own vehicle and its contents so they can have it repaired or replaced in case of accidents or damage. This is generically called Physical Damage, and is not required by law. It includes:
  1. Collision coverage to repair or replace your vehicle if it is in an accident or overturns.
  2. Comprehensive coverage to pay for any other damage: fire, theft, hail, vandalism, etc.

The insurance company pays the actual cash value of the loss.

- Medical Expense - This covers you and passengers in your vehicle for bodily injuries suffered in an accident, no matter who is at fault. This coverage also covers you and your insured family members (your household) in any traffic accident, including in other cars, on bicycles, and on foot. There is a per-person limit for this coverage, usually \$5,000 or \$10,000.

### Reducing Your Costs

You may be able to lower your premiums in these ways:

- Stay on a parent's policy: If you're under 25, you may be eligible to stay on your parent's policy, which could be less expensive for you.
- Ask your agent for safe driver or other discounts.
- Pay a higher deductible: You can lower your premium by raising your deductible (the set amounts you pay any time you file a claim on your insurance).

Should I have a high or low deductible?

Automobile deductibles range from \$100 to \$1,000 or more. Generally safe drivers would benefit from carrying a higher deductible because they pay lower premiums all the time and only rarely have to pay the deductible. They could then invest the savings. If your vehicle is new or its repair costs are high, you would have a high repair bill no matter how minor the damage. Therefore, a lower

deductible, perhaps \$250, is probably a good idea. If you have an older, less expensive car, your repair costs would be low. With any deductible, you'll probably pay for most of the repairs for any accident. So you should keep a high deductible, perhaps \$500, to have low premiums and to replace the car in case it is totaled. You can also lower your premiums by reducing your coverage. If you drive an old car you may not even repair it if it is damaged. If you have savings and other transportation backup, you could drop the Collision coverage. Weigh the cost of the coverage you want to drop against what you'd have to pay if something happened. Could you afford to cover the loss without insurance?

The following example (used for illustrative purposes only) shows the advantages and disadvantages of a high deductible versus a low deductible:

Total Cost of Incident	Deductible (You pay)	Insurance Pays	Monthly Premium
\$3000.00	\$1000.00	\$2000.00	\$100.00
\$3000.00	\$100.00	\$2900.00	\$200.00

### Should you file a claim?

People often question whether they should file a claim out of fear that it will lead to higher insurance premiums, especially in the case of a minor automobile accident. As a rule, it is always best to notify your agent. Ask if your rates will increase if you file a claim, and then weigh the cost of paying a loss out of your pocket against the higher premium. You should be aware, however, that paying your own money for minor property damage losses suffered by others can be viewed as an admission of liability should you later be sued for bodily injury losses that were not evident at the time of the accident.

Another way to keep down your premium costs is to stay out of trouble with your vehicle. Insurance companies raise premiums if:

- You get frequent and/or serious traffic tickets
- You file a lot of claims for damage

- You let others drive your vehicle, which gets damaged

### **If You're Deployed**

If you will be deployed and will not use your car for several months or more, DO NOT drop your coverage. If you still owe on the vehicle, the bank REQUIRES you to keep it insured, and even while in storage the vehicle could be damaged or stolen. In addition, your rates are likely to go up when you try to reinstate or repurchase insurance.

For those deploying overseas who want to take a car, be sure to check with the base office which handles overseas transfers for information on requirements for driving and insuring your vehicle in another country. Your insurance company may not even cover vehicles there. You may decide it's easier to leave your car in the U.S.

Let's review the things to do when buying vehicle insurance.

- Look for an agent who will explain the details patiently.
- Shop for the coverage you need at the lowest cost.
- Independent agents can sell policies from more than one company, and can help compare policies.

### **B. Life Insurance**

The purpose of life insurance is to help cover financial losses after the death of a money earner. Life insurance lets you care for people who were dependent on your income.

### **Do you need life insurance?**

- You have young children who have not completed their education
- Your spouse may need more time/education to be self-supporting
- You provide support for parents or a disabled family member
- You have significant debts and no means to pay them off



If you checked even one of these items, you may want to consider some life insurance. The need for life insurance varies as your life changes. You should re-evaluate your needs regularly. Consider it a responsibility to those you love.

If you DO need life insurance, the next question is do you have any life insurance now? The military covers some of your family's immediate financial needs through several types of assistance. Upon the death of a married active-duty member of the U.S. armed forces, any dependent survivors will automatically receive several types of financial support from the government. The military will pay most burial costs and provide some support to dependent survivors. Visit the Veteran's Administration homepage at <http://www.va.gov> for more information about this assistance.

We'll discuss the types of assistance provided, which should be included in any needs assessment determining your insurance requirements. Let's review this together. When a servicemember dies, a **Casualty Assistance Calls Officer (CACO)** is assigned to help surviving family members during the readjustment period following the death of the servicemember. The CACO will also make all funeral and burial arrangements for the family. The military will pay for the cost of a basic funeral. The government will also provide transportation for family members to the funeral and back home. The immediate family is also provided a free move from the duty station to a new location if they wish. Finally, the family is given up to 3 months of Basic Allowance for Housing (BAH) or is allowed to stay in military quarters for 90 days before they would have to move. The surviving spouse will also receive **Dependency & Indemnity Compensation (DIC)**. This is (currently) an \$833 per month payment (plus \$210 per dependent child). A surviving spouse or children can receive both DIC and Social Security. However, receipt of DIC does reduce payments from the Survivor Benefit Plan, a savings-for-survivors account, in which you may have participated.

The military services offer very inexpensive life insurance called Servicemen's Group Life Insurance (SGLI). When you go on active duty you "automatically" sign up for coverage for \$9 per month (.09 cents per \$1,000). That's \$108 annually for \$100,000 - an excellent value. Unless you refuse the coverage, the premiums are then

deducted from your paycheck. The only thing you need to do is fill out a form at your personnel office designating the beneficiary (the person who would receive the payment).

If you have dependents, you should strongly consider increasing your life insurance coverage. SGLI can be purchased for amounts up to \$250,000. SGLI is generally less expensive than a “civilian” policy, and is easy to qualify for and arrange. For some military jobs, this may be the only life insurance you can get. Non-military insurers may think certain occupations are too dangerous to insure. You may even decide that you need more than the maximum SGLI insurance, depending on the size of your family and other personal considerations. If so, consider purchasing additional insurance outside of the military.

Is your situation balanced? Your insurance needs are for income, final expenses and funds for lifestyle adjustments. Do your death benefits cover these needs? How much more do you need? The first thing you would do is list all of your family’s financial needs. Next, you’d list the financial assets that your survivors will have. Last, you’d subtract what they’ll have from the amount you estimate the survivors will need. If there is a difference, this total will show how much they’ll be short. Then you’ll know if you need more life insurance.

Do you need insurance?	
Family’s Financial Needs - <u>Survivor’s Financial Assets</u> =                   ?	← if positive then you may want to consider insurance

Term vs. Cash Value: If you decide that you do need life insurance, and look outside of SGLI, you should know the two primary types available, and how to compare costs. There are two general “types” of life insurance: term and cash-value.

Term life insurance is simple:

- It covers you only for a specified time period (a “term” of 1, 5, 10, 20 years)

- It pays benefits only if the insured person dies within that time period
- The only payback from term insurance is the death benefit
- It is the cheapest, simplest life insurance for a young person, when most people need life insurance, but gets more expensive as you get older

The other general type is “cash-value” life insurance, which:

- Pays a death benefit
- Slowly builds cash value in the policy, which you can later withdraw or borrow against
- Can vary in features and be called “permanent life”, “whole life”, or “universal life”

This may sound like a better deal, so what’s the catch? The reality is that you pay for fees and life insurance first, at a higher than necessary cost, and then you slowly build cash value. So it’s a more expensive way to do either insurance OR savings.

How do you choose among all these varieties? Here is what many financial experts recommend:

- Term insurance is the most economical way to buy life insurance
- Cash value policies are expensive combinations of insurance and savings
- If you need life insurance, buy term insurance at the lowest cost possible and invest the difference between what you would pay for term insurance and more expensive types of insurance

Life cycle need for life insurance is another concept financial experts use. The need for life insurance is usually the greatest when you are younger and have more people depending on your income. Term insurance is cheaper while you are younger and gets more expensive as you age. Cash value cost stays the same. Buy term and invest the rest means buy the cheaper insurance so that by the time it becomes more costly you will no longer need outside insurance. You will have invested the difference each year and are now self-insured.

## Per-Unit Pricing

Most insurance is sold per “unit” of coverage. For life insurance, you should look for the lowest price per \$1,000 of coverage per year. This translates into your annual premium (what you pay each year). For example, if you want \$100,000 of coverage, and the annual cost per \$1,000 is \$1, you’d multiply 100 times \$1 to get \$100 for your annual premium. You should ask, “cost per \$1,000,” as well as what fees are charged, every time you check into a life insurance policy. Keep in mind that the lowest price may not necessarily be the best deal; if your insurance company goes bankrupt then its low premiums won’t do you much good.

It pays to shop for life insurance! Here are some basic guidelines for buying life insurance:

- Shop and compare cost per \$1,000 of coverage per year. Prices vary widely!
- Ask about commissions and fees
- Avoid policies that charge both commission and a “back-end load” (fee at withdrawal)
- Check the financial stability of any insurance company through a ratings service

Insurance companies are rated by independent rating services, such as Best’s Insurance Reports <http://www.ambest.com> and Moody’s <http://www.moody.com>. These reports are available in most libraries. A rating of A+, Aaa, or AAA usually indicates a superior rating which means financial stability of the company. This information is very important to you. A strong financial rating coupled with many years in the business will likely mean that if you have a claim some years down the road (hopefully very many years when discussing life insurance), the company will be able to hold up its end of the policy (contract) and pay out the benefits.

The key points we have covered on life insurance are that it is:

- Highly recommended for anyone with dependents who rely on their income

- Can be a “term” policy or a “cash-value” policy
- Should be compared by price per \$1,000 of coverage
- Varies in cost among insurance companies

### **C. Personal Property Insurance**

Property insurance covers the loss of, or damage to, your possessions, such as a home, furnishings, clothes, jewelry, electronics, etc. How do you decide if you need insurance on these things? Ask yourself this question: could I afford to lose these things and replace them without the help of insurance? For most people the answer is “No.” Remember, also, that if you are paying for any item on credit, even if it is damaged or destroyed, you will still owe the creditor the balance of your loan!

Renters should consider Renter’s Insurance

People who rent often have no insurance on their belongings. This can be an expensive mistake! Most people should get at least a small renter’s property insurance policy so that they are not financially devastated if something like a fire occurs. If you think you don’t have much to insure, make a list of everything you have and record its replacement cost (what it would cost to replace it today). Can you afford to lose it all? A basic renter’s personal property policy for about \$15,000 coverage probably costs less than \$150 per year. Having smoke detectors, fire extinguishers, or a burglar alarm helps reduce the premiums.

Homeowner’s and Liability Coverage

Mortgage companies require homeowners to have a homeowner’s insurance policy until the mortgage is paid in full. A homeowner’s policy combines property insurance and liability into a single-package policy. A homeowner’s policy (like any personal property policy) should insure all property for its replacement cost. Check for things a standard homeowner’s policy covers:

- Property damage to the dwelling and other structures on the property

- Damage to personal property and dwelling contents
- Liability against damage to other people and property when on your property
- Your expenses if you cannot live in the home for some reason

If you deploy, do you need to keep your insurance? If you own a home and have a mortgage, you are required to keep it insured (and you'd certainly be wise to keep it after that!). But if you had renter's insurance and put your things in storage, you may be tempted to drop your policy. **DON'T DROP IT!** Your things can be stolen or damaged no matter where you have them. Ask your insurance agent about keeping some coverage on your belongings when you're away. For personal possessions, you will need some kind of documentation to prove the items' value. The best documentation is photos and receipts. Photograph or videotape all valuable property.

As with any type of insurance, it pays to shop around. Be prepared with your list of possessions and their replacement values. Call or visit several agents and ask them to explain all policy coverage, exclusions, and costs. Be sure to ask for replacement value coverage.

Who should have insurance on their personal possessions?

Anyone who can't afford to lose everything they own. The crucial items to remember about Personal Property Insurance, which covers your belongings, are:

- Homeowner's Insurance is required if you have a mortgage
- Renter's Insurance is critical if you rent and have even a few possessions
- Liability Insurance is part of homeowner's policies
- You should comparison shop for property insurance and ask for discounts

## **D. Health And Disability Insurance**

Medical costs today are very high, and the cost of a serious illness or injury can be financially devastating. Everyone should have some

health insurance, especially what's known as "major medical" coverage. As a member of the armed services, all of your health care and most of your dependent family members' health care is covered at no cost to you. Wherever you are in the world, as a member of the U.S. military you can receive care at a U.S. military medical facility if one is available. If not, you can go to a civilian facility and receive care for little or no out-of-pocket expense.

A soldier's dependent family members can skip the military providers and go to civilian care facilities for health care by enrolling in the Civilian Health and Medical Program of the Uniformed Services (CHAMPUS)/Tricare program. This can be used in addition to use of the military care facilities. **You must sign up for CHAMPUS/Tricare.** If you have dependents and want them to be covered under CHAMPUS or Tricare, you must enroll them in the program.

**Defense Eligibility Enrollment Reporting System (DEERS)** is the nationwide computerized data bank that contains the names of all active duty and retired military sponsors and their medical, CHAMPUS, Tricare eligible family members. When applying for a dependent ID card, your family member will be automatically enrolled. Since they don't have ID cards, you must enroll dependent children under the age of 10. Remember to take your marriage license and child's birth certificate when you go to enroll your family members. To verify DEERS enrollment, call toll-free (800) 538-9552. In California, call (800) 334-4162 and in Alaska and Hawaii call (800) 527-5602. You will need to have your (the soldier's) Social Security number available when you call.

As an active duty member of the U.S. Armed Forces, the government automatically provides your medical expenses and disability income protection. Your dependent family members can also use military health facilities at no cost. By enrolling in CHAMPUS/Tricare, your family can also use civilian facilities. If your family depends heavily on a non-military spouse's income, the spouse should consider buying disability insurance.

Insurance is a necessity for most people. Vehicle liability insurance is required by states and military facilities. Life insurance helps support

family members who depended on your income. Homeowners MUST have insurance; home renters need it also! Soldier health costs are fully paid by the government. Dependents' health care costs are nearly all paid by the government. So as you can see, active duty soldiers are provided a number of insurance benefits. It is important to remember these benefits that you are already receiving at little or no cost to you when determining any further insurance needs which you must pay for out of pocket.

### **Helpful Links and Recommended Reading**

[www.ambest.com](http://www.ambest.com)

[www.moodys.com](http://www.moodys.com)

[www.va.gov](http://www.va.gov)

**Dictionary of Insurance Terms (Dictionary of Insurance Terms, 4th Ed)** -- by Dr. Harvey W. Rubin

**Insurance for Dummies** -- by Jack Hungelmann